

Message Text

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SUBJECT: REVISED 1976 ECONOMIC POLICY CONDITIONS FOR ITALY

REF: (A) EC BRUSSELS 2650, (B) EC BRUSSELS 2319, (C) EC BRUSSELS 1384

1. BEGIN SUMMARY: THE EC FINANCE COUNCIL DECIDED ON MARCH 15 TO ADOPT REVISED ECONOMIC POLICY CONDITIONS FOR ITALY WHICH ARE REQUIRED FOR THE EC \$1 BILLION LOAN TO ITALY. THESE CONDITIONS ARE SOMEWHAT MORE STRINGENT THAN THOSE ADOPTED BY THE EC MONETARY COMMITTEE IN NOVEMBER 1975 AS PART OF THE EC MEDIUM-TERM CREDIT TO ITALY. COMMISSION OFFICIALS ARE NOT OPTIMISTIC THAT THE GOI WILL BE ABLE TO MEET THESE CONDITIONS IN VIEW OF STRONG DOMESTIC COST-PUSH PRESSURES AND THE GOVERNMENT'S WEAKNESS. THEY ALSO HAVE REVISED DOWNWARD THEIR FORECAST OF ITALIAN GROWTH EXPECTATIONS. END SUMMARY.

2. THE FOLLOWING ARE EXCERPTS FROM THE COUNCIL'S DECISION, WHICH IS GENERALLY CONSISTENT WITH BUT MORE DETAILED THAN THE INFORMATION IN REF. B:

-ARTICLE 1

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THE LOAN GRANTED TO THE ITALIAN REPUBLIC BY DECISION 76/ /EEC

SHALL BE SUBJECT TO THE FOLLOWING CONDITIONS CONCERNING THE ECONOMIC
POLICY MEASURES TO BE TAKEN BY THAT MEMBER STATE.

ARTICLE 2

1. THE FOLLOWING CONDITIONS SHALL BE OBSERVED DURING 1976:

(A) TOTAL CENTRAL GOVERNMENT EXPENDITURE MUST BE LIMITED
TO LIT 39,700,000 MILLION IN THE 1976 CALENDAR YEAR;

(B) THE DEFICIT ON TREASURY TRANSACTIONS, AS DEFINED IN
ARTICLE 6 (3) OF DIRECTIVE 74/637/EEC, MUST NOT
EXCEED LIT 13,800,000 MILLION, THROUGH AN INCREASE
IN TAXATION, IF NECESSARY;

(C) THE FINANCING OF THE DEFICIT ON TREASURY TRANSACTIONS BY
THE MONETARY AUTHORITIES MUST BE LIMITED, IF BY
LEGISLATIVE MEANS, TO LIT 5,700,000 MILLION IN THE 1976
CALENDAR YEAR;

(D) THE GROWTH IN TOTAL LENDING, AS DEFINED IN ARTICLE 6
OF DIRECTIVE 74/637/EEC, MUST NOT EXCEED LIT 29,500,000
MILLION IN THE 1976 CALENDAR YEAR.

2. THE COUNCIL, ACTING ON A PROPOSAL FROM THE COMMISSION, SHALL IN
GOOD TIME FIX THE CONDITIONS TO BE OBSERVED FOR THE SUBSEQUENT
YEARS OF THE LOAN PERIOD.

ARTICLE 3

THE ITALIAN GOVERNMENT SHALL MAKE ALL POSSIBLE EFFORTS TO KEEP
THE RISE IN INCOMES WITHIN LIMITS COMPATIBLE WITH THE INTERNAL AND
EXTERNAL EQUILIBRIUM OF THE ECONOMY.

ARTICLE 4

THE CONDITIONS FIXED IN ARTICLE 2 SHALL AMEND, TO THE
EXTENT THAT THEY DIFFER FROM, THE CONDITIONS PROVIDED FOR IN
DIRECTIVE 75/784/EEC.

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ARTICLE 5

BEFORE THE END OF APRIL 1976 INTERMEDIATE OBJECTIVES SHALL
BE ESTABLISHED BY AGREEMENT BETWEEN THE ITALIAN AUTHORITIES AND
THE COMMISSION IN RELATION TO THE MEASURES LAID DOWN IN
ARTICLE 2, EXCEPT FOR THAT SET OUT IN ARTICLE 2 (1)(B)."

3. COMMISSION OFFICIALS BELIEVE THESE CONDITIONS ARE QUITE
STRINGENT. THE RECENT DEPRECIATION OF THE LIRA, COMBINED WITH

POSSIBLE LARGE WAGE INCREASES THIS YEAR, COULD CREATE STRONG COST-PUSH PRESSURES. THESE PRESSURES WILL ADD TO THE GOI DIFFICULTIES IN MEETING THESE CONDITIONS. THEY BELIEVE THE GOI PERHAPS ACCEPTED THESE MORE STRINGENT CONDITIONS TOO QUICKLY. THEY SPECULATE THAT THIS MAY INDICATE A WILLINGNESS BY SOME ITALIAN OFFICIALS TO GO ALONG WITH THE CONDITIONS IN ORDER TO OBTAIN EC AGREEMENT TO THE LOAN WITHOUT ANALYZING WITH SUFFICIENT CARE THE POSSIBLE IMPLICATIONS OF THESE CONDITIONS. THE COMMISSION, NEVERTHELESS, PLANS TO SET UP PROMPTLY, INTERMEDIATE OBJECTIVES WHICH WOULD BE DESIGNED TO ASCERTAIN ON A QUARTERLY BASIS ITALIAN PERFORMANCE IN MEETING THE CONDITIONS. THE OFFICIALS SAY THE IMF WILL LIKELY ADOPT THE SAME CONDITIONS FOR ITS PROPOSED STANDBY AGREEMENT WITH ITALY.

4. IN LIGHT OF THE REVISED CONDITIONS AND RECENT DEVELOPMENTS, THE COMMISSION HAS REVISED DOWNWARD ITS 1976 FORECASTS FOR THE ECONOMY (SEE REF C). THEY NOW ESTIMATE THAT GDP WILL GROW IN REAL TERMS 0.5 TO 1 PERCENT RATHER THAN ITS EARLIER FORECAST OF 2.5 PERCENT. THE GDP PRICE DEFLATOR SHOULD RISE 16.5 PERCENT BASED ON A HYPOTHETICAL DEPRECIATION OF THE LIRA OF 12 PERCENT THIS YEAR. THE VOLUME OF EXPORTS IS ESTIMATED TO RISE 7.5 PERCENT OVER 1975 AND THE GOI'S BOP DEFICIT ON CURRENT ACCOUNT IS FORECASTED TO REACH 300 TRILLION LIRA THIS YEAR. UNEMPLOYMENT BASED ON DATA FROM THE NATIONAL STATISTICS INSTITUTE WILL RISE 10 PERCENT THIS YEAR REACHING AN AVERAGE OF ABOUT 700,000 OF FULL-TIME UNEMPLOYED. HINTON

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